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INFO RUEHFK/AMCONSUL FUKUOKA 8202
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RUEHNH/AMCONSUL NAHA 0546
RUEHOK/AMCONSUL OSAKA KOBE 2015
RUEHKSO/AMCONSUL SAPPORO 8701
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UNCLAS SECTION 01 OF 04 TOKYO 000039

SENSITIVE
SIPDIS

TREASURY FOR DOHNER, WINSHIP, AND FOSTER
STATE FOR E, EEB AND EAP/J
NSC FOR DANNY RUSSELL AND JIM LOI
STATE PASS TO USTR FOR AUSTR CUTLER, BEEMAN, LEE AND
HOLLOWAY

E.O. 12958: N/A
TAGS: [ECON](#) [EFIN](#) [JA](#)
SUBJECT: HATOYAMA CABINET APPROVES FY2010 BUDGET

REF: A. TOKYO 00018
 [1](#)B. TOKYO 00025
 [1](#)C. 2009 TOKYO 02819
 [1](#)D. 2009 TOKYO 02464

[1](#)1. (SBU) Summary: The Hatoyama Cabinet approved the central government's initial budget for FY2010 (April 2010 - March 2011) on December 25, clearing the way for its submission to the Diet. This is the first full budget formulated by the Hatoyama Administration since it came to power in September [1](#)2009. The initial FY2010 general account budget of JPY92.3 trillion (US\$1.0 trillion) represents a 4 percent increase over the initial FY2009 budget, but is still 10 percent smaller (about JPY10 trillion (US\$109 billion) or 2.2 percent of GDP) than the revised FY2009 budget, inclusive of the two FY2009 supplemental budgets.

[1](#)2. (SBU) FY2010 tax revenues are projected to remain weak, rising only 1.5 percent from FY2009. Consequently, the budget assumes that Japanese government bond (JGB) issuances will exceed tax revenues for the second straight year. The budget contains JPY3.1 trillion (US\$34 billion) in policy measures promised in the DPJ's "manifesto" (policy platform) issued in the run up to the August 2009 Lower House election. The budget bills will be submitted to the Diet in January. Final Diet approval is likely in late March. End Summary.

Competing Budgetary Priorities

[1](#)3. (SBU) In compiling the FY2010 budget, the Hatoyama Cabinet sought to navigate between two competing policy priorities: demonstrating the DPJ's fiscal discipline while avoiding premature withdrawal of fiscal stimulus. The combined FY2010 general account and FILP (Fiscal Investment and Loan Program) outlays are equivalent to 23 percent of GDP in FY2010. While this represents a contraction of 3.4 percentage points (pp) from FY2009, total outlays are still a full 2.1 pp higher than the average of the previous ten years (FY2000-2009). The government also appears to be counting on the assumption that most of the JPY7.2 trillion (US\$ 78 billion) in new spending included in the second FY2009 supplemental budget will only actually impact the economy in FY2010.

General Account Expenditures

14. (SBU) FY2010 general account expenditures for FY2010 total JPY92.3 trillion (US\$1 trillion), a 4 percent increase over the initial FY2009 budget. This partly reflects a 6 percent increase in revenue sharing with local governments due to their worsening fiscal condition. Debt service costs are also projected to increase 2 percent, under the assumption that the ten-year JGB yield averages 2.0 percent in FY2010. Social security spending is set to increase 10 percent and accounts for over half (51 percent) of total discretionary ministerial budget spending. This increase is largely due to the introduction of a child allowance program paying JPY13,000 (US\$141) per month for each child until graduation from middle school, a key DPJ electoral pledge. In contrast, public works spending is set to decline a record 18 percent to JPY5.8 trillion (US\$63 billion), consistent with the Hatoyama Cabinet's intent to shift fiscal resources "from (construction) concrete to households." Spending on official development assistance (ODA) has been cut 8 percent from the initial FY2009 budget to JPY619 billion (US\$6.7 billion), the eleventh consecutive annual decrease on an initial-over-initial budget basis. Like last year, the FY2010 general account budget contains JPY1.35 trillion (US\$14.6 billion) in reserves, including JPY1.0 trillion (US\$10.9 billion) to cope with economic shocks. In addition, the FY2010 budget will repay JPY0.7 trillion (US\$7.6 billion) borrowed in FY2008 from the debt consolidation special account (a sinking fund) to cover smaller-than-estimated tax revenues.

15. (SBU) (Note: The general account budget consists of two mandatory spending items -- debt service costs and revenue

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sharing with local governments -- as well as discretionary ministerial budget spending such as social security and public works. End note.)

16. (U)

FY2010 General Account Budget Expenditures

	JPY trillion	percent change from initial FY2009
TOTAL	92.3	4.2
Debt Service Costs	20.6	2.0
Revenue Sharing with Local governments	17.5	5.5
Ministerial Budget Spending	53.5	3.3
Social Security	27.3	9.8
Education and Science	5.6	5.2
Military Pensions	0.7	-9.3
National Defense	4.8	0.3
Public Works	5.8	-18.3
Economic Cooperation	0.6	-7.5
Small Businesses	0.2	1.1
Reserves	1.4	0.0
Other	7.2	6.1
Repayment to FY2008 Settlement Fund	0.7	n/a

(Note: ODA includes spending budgeted under Economic Cooperation, as well as under other budget categories. End note.)

17. (U)

FY2010 General Account Budget

	Initial FY2010	Change from Initial FY2009	Revised FY2009

	(trillion)	(percent)	
TOTAL EXPENDITURES	92.3	4.2	-10.0
Ministerial Budgets	53.5	3.3	-19.9
Social Security	27.3	9.8	-5.3
Public Works	5.8	-18.3	n/a
Other Discretionary	20.4	3.0	n/a
Debt Service	20.6	2.0	7.3
Revenue Sharing with Local Governments	17.5	5.5	5.5
Repayment to FY2008 Settlement Fund	0.7	n/a	n/a
TOTAL RECEIPTS	92.3	4.2	-10.0
Tax Revenues	37.4	-18.9	1.5
Other receipts	10.6	15.8	-13.4
Government Bond Issuance	44.3	33.1	-17.1

18. (U)

FY2009 General Account Budget

	Initial FY2009	FY2009 with Supplementals
	(trillion)	
TOTAL EXPENDITURES	88.5	102.6
Ministerial Budgets	51.7	66.7
Social Security	24.8	28.8
Public Works	7.1	n/a
Other Discretionary	19.8	n/a
Debt Service	20.2	19.3
Revenue Sharing with Local Governments	16.6	16.6
Repayment to FY2008 Settlement Fund	0.0	0.0

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TOTAL RECEIPTS	88.5	102.6
Tax Revenues	46.1	36.9
Other receipts	9.2	12.2
Government Bond Issuance	33.3	53.5

Measures Contained in the DPJ Manifesto

19. (SBU) The FY2010 general account budget contains a total of JPY3.1 trillion (US\$33.7 billion) in policy measures promised by the DPJ ahead of last August's Lower House election. This is roughly JPY3.8 trillion (US\$41.3 billion) smaller than the budget requests made in October by individual ministries to conform to the DPJ's manifesto. The decrease is largely a result of the Hatoyama Cabinet's decision not to eliminate the surcharge rates on four road-related taxes from April 2010 (Ref A). Instead, the surcharge rates on three road-related taxes (gasoline tax, diesel oil delivery tax, and automobile acquisition tax) will be replaced by new "special" rates that result in no change in the tax burden. The remaining fourth surcharge rate on the automobile tonnage tax will be halved from JPY3,800 to JPY1,900 (US\$41 to US\$21) per half ton from April 2010.

10. (U) The FY2010 budget does include:

-- A new monthly child-rearing allowance of JPY13,000 (US\$141) in FY2010 to each child until graduation from middle school, with no household income ceiling.

-- The elimination of designated highway tolls.

-- A JPY0.6 trillion (US\$6.5 billion) income support subsidy program for rice farmers designed to make up the difference between the cost of production and sales price.

-- Making public high school effectively free, as well as providing JPY120,000 to JPY240,000 (US\$1,304 to US\$2,609) per year for each private high school student, depending on

household income levels.

¶11. (U)

Measures Promised in DPJ's Manifesto

	Requested	Actually Budgeted

	(trillion)	
TOTAL	6.9	3.1
Spending Measures	4.4	2.9
New Monthly Child Allowance	2.3	1.7
Highway Tolls Elimination	0.6	0.1
Rice Farmers Income Support	0.6	0.6
Free High School	0.5	0.4
Employment Measures	0.3	0.02
Pension Records Problems	0.1	0.1
Tax Measures	2.5	0.2
Road-related Tax Surcharges Elimination	2.5	0.2

(Note: Local governments will shoulder some costs for the child allowance program. End note.)

General Account Receipts

¶12. (SBU) MOF projects FY2010 tax revenues at JPY37.4 trillion (US\$407 billion), a 1.5 percent increase from FY2009. Given this weak tax revenue growth, MOF plans to issue JPY44.3 trillion (US\$482 billion) of new JGBs in FY2010, barely meeting the Hatoyama Cabinet's policy target of limiting JGB issuance in the initial budget to "about JPY44 trillion (US\$478 billion)" (equivalent to the FY2009 initial budget plus the first FY2009 supplemental budget). As a result, the total amount of JGBs issued in FY2010 is projected to exceed tax revenues for the second year in a

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row. As for non-tax receipts, MOF will transfer to the general account budget JPY4.8 trillion (US\$52 billion) in retained earnings from the Fiscal Loan Fund Special Account and, consistent with past years, JPY2.9 trillion (US\$32 billion) in retained earnings from the Foreign Exchange Special Account.

Overview of FILP

¶13. (U) The FY2010 FILP (the so-called "second budget") calls for total outlays of JPY18.4 trillion (US\$200 billion), up 16 percent from the initial FY2009 level, but down 22 percent from the final FY2009 level inclusive of the two FY2009 supplemental budgets. FILP lending to government-affiliated financial institutions and public works related agencies will decline 33 percent and 42 percent from their final FY2009 levels, respectively. Allocations to local governments will increase 10 percent. FILP financing is mainly provided through FILP bonds (JPY13.5 trillion or US\$147 billion) and government-guaranteed bonds (JPY4.8 trillion or US\$52 billion).

¶14. (U)

FY2010 Fiscal Investment and Loan Program

	Initial FY2010	Change from Initial FY2009	Revised FY2009

	(trillion) (percent)		
TOTAL OUTLAYS	18.4	15.7	-22.2
Government affiliated			

financial institutions	10.5	26.3	-33.2
Public works agencies	0.6	-30.8	-42.5
Local governments	4.3	10.3	10.3
Other	3.0	5.7	-0.4
TOTAL FUNDING	18.4	15.7	-22.2
FILP bonds	13.5	12.6	-25.4
Government-guaranteed bonds	4.8	26.5	-6.6
Other	0.1	-14.4	-74.5

15. (U)

FY2009 Fiscal Investment and Loan Program

	Initial FY2009	FY2009 with Supplementals

	(trillion)	
TOTAL OUTLAYS	15.9	23.6
Government affiliated		
financial institutions	8.3	15.7
Public works agencies	0.8	1.0
Local governments	3.9	3.9
Other	2.8	3.0
TOTAL FUNDING	15.9	23.6
FILP bonds	12.0	18.1
Government-guaranteed bonds	3.8	5.1
Other	0.1	0.4

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